No. 541.

Supreme Court of the United States

OCTOBER TERM, 1939.

GERTRUDE VANDERBILT WHITNEY and CORNELIUS VANDERBILT, as Executors of the Last Will and Testament of ALICE G. VANDERBILT, Deceased, *et al.*,

Appellants,

vs.

STATE TAX COMMISSION OF THE STATE OF NEW YORK.

BRIEF FOR THE APPELLANTS.

ARTHUR A. BALLANTINE,
ROY C. GASSER,
THOMAS B. GILCHRIST,
HORACE R. LAMB,
LEO GOTTLIEB,
Counsel for Appellants.

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GERTRUDE VANDERBILT WHITNEY and CORNELIUS VANDERBILT, as Executors of the Last Will and Testament of ALICE G. VANDERBILT, deceased, and said CORNELIUS VANDERBILT, individually, GLADYS SZECHENYI, CATHLEEN VANDERBILT LOWMAN, GLORIA LAURA MORGAN VANDERBILT, infant, and THOMAS B. GILCHRIST, as General Guardian of the property of said infant,

Appellants,

against

STATE TAX COMMISSION OF THE STATE OF NEW YORK,

Appellee.

OPINIONS OF THE STATE COURTS

The opinion of the Surrogate (R. 66) is reported in 163 Misc. 667, 297 N. Y. Supp. 554. The opinion of the New York Court of Appeals (R. 86) is reported in 281 N. Y. 297, 22 N. E. (2d) 379.

JURISDICTION

The judgment of the Court of Appeals was rendered July 11, 1939 (R. 84). The appeal to this Court was taken October 10, 1939, and probable jurisdiction was noted by this Court in an order dated December 11, 1939. The jurisdiction of this Court rests upon Section 237(a) of the Judicial Code, as amended by the Acts of February 13, 1925, January 31, 1928 and April 26, 1928.

STATEMENT

The decision from which this appeal is taken sustained against constitutional objections the validity of an estate tax the measure of which included $5,285,572 of trust property (R. 15, 67) in which the decedent had never had any beneficial interest, either at death or at any other time. The sole connection of the decedent with such property was that she exercised a limited or special, and wholly non-beneficial, power of appointment over such property.

Alice G. Vanderbilt, the decedent in the present case, was the widow of Cornelius Vanderbilt. Cornelius Vanderbilt died on September 12, 1899, leaving a will whereby he created a trust for the payment of an annual income of $250,000 to his wife for her life. He gave the remainder of this trust fund to four of his children and their issue (and to any child born after his death) in such proportions as his wife might appoint in her will; in default of appointment, the trust fund was to be divided equally (R. 40).

The decedent was thus given authority to exercise a "*special power in trust*" within the meaning of the applicable New York statute (Real Property Law, Sections 135(1), 138(1)). She could not have exercised the power in any way for her own benefit; not only was she unable to appoint in favor of any persons except the four children or their issue, but, as the highest State Court has determined in this case, she was forbidden to seek or accept any reward or compensation for exercising the power in a particular way (R. 87). It is clear, therefore, that the decedent never had any beneficial interest in the remainder interest in the trust fund created by her husband's will, and it is

this remainder interest, ripened into full ownership by the extinction of the decedent's life interest, which is involved in the present case.

The decedent died on April 22, 1934, a resident of New York County (R. 9, 14). By her will she carried out the trust imposed on her by her husband's will, by exercising the limited power of appointment thus delegated to her. She appointed the remainder interest in the trust fund as follows (R. 30-1):

> $150,000 to her daughter Gertrude V. Whitney;
>
> $500,000 to the issue of her deceased son Alfred G. Vanderbilt;
>
> One-third of the balance to the issue of her deceased son Reginald C. Vanderbilt (Cathleen Vanderbilt Lowman and Gloria Laura Morgan Vanderbilt); and
>
> The remaining two-thirds of the balance to her daughter Gladys Szechenyi.

The entire trust property, valued at $5,935,572, was included in the decedent's taxable estate in the first instance by the Tax Appraiser (R. 15). In the Surrogate's Court, however, there was excluded from the taxable estate so much of the fund as had been appointed to Gertrude V. Whitney and the issue of Alfred G. Vanderbilt, *viz.*, $650,000, on the ground that these appointees received less than they would have received if the power of appointment had not been exercised, and therefore these appointees were to be deemed to have taken, not upon the exercise of the power by the decedent, but under the will of the grantor of the power (R. 67). See *Matter of Duryea*, 277 N. Y. 310 (1938). The balance of the appointed property, however, *viz.*, $5,285,572, was held by the

Surrogate to have been properly included in the decedent's taxable estate, and, after an intermediate appeal, this decision was affirmed by the State Court of last resort, the New York Court of Appeals (R. 84-5).

The total increase in tax resulting from the inclusion of such trust property in the decedent's taxable estate was about $852,000 (see pp. 38-9 below). Since the tax rate increases progressively with an increase in the total amount of the taxable estate, the aggregation of this property with the decedent's own property in determining the amount of the taxable estate has resulted in the application of higher rates in respect of all of the property included in the taxable estate. Thus, the tax in respect of the decedent's own property has been increased by approximately $163,000 by the application of the higher rates resulting from the inclusion in the taxable estate of the trust property (see p. 39 below). If the trust property had been taxed in the estate of the owner of the property, Cornelius Vanderbilt, who created the trust and granted the power of appointment, instead of being taxed in the estate of the decedent, the tax in respect of this property under the death tax statute in force at the time of the death of such owner (1899) would have been only about $30,000.

THE STATUTORY PROVISIONS

The tax was imposed under Article 10-C of the New York Tax Law (Cons. Laws, c. 60). This Article was enacted in 1930 (L. 1930, c. 710) and took effect on September 1, 1930. For all persons dying after that date, it substituted for the death tax previously in force in New York, which was a tax of the kind re-

ferred to in this brief as a *legacy tax*, a new death tax of the kind referred to as an *estate tax*. Although, as appears more fully below, the distinction between these two wholly different kinds of death tax is well recognized, the terms used to describe them are not uniform. (See dissenting opinion of Mr. Justice Roberts in *Coolidge* v. *Long*, 282 U. S. 582 (1931), at p. 608). Since the distinction is of great importance in the present case, it is well to make clear at the outset the terminology used in this brief to designate the two kinds of death tax.

The term "legacy tax" is used to refer to a death tax imposed upon the right of the recipient to receive property on a death, and measured by the amount of property so received. The term "estate tax" is used to refer to a death tax imposed upon the right of the decedent to transmit his property at death, and measured by the amount of property so transmitted. If a legacy tax is scaled at progressive rates, as virtually all death taxes now are, the rates advance as the amount received by any one beneficiary increases. In the case of a progressive estate tax, however, the rates advance as the total amount of the taxable estate, *i.e.*, the property transmitted by the decedent, increases. As phrased in the early leading case of *Knowlton* v. *Moore*, 178 U. S. 41 (1900), the distinction is between "a tax on the interest to which some person succeeds on a death", here called a legacy tax, and "a tax on the interest which ceased by reason of the death", here called an estate tax.

The estate tax enacted by Article 10-C was closely modeled upon the Federal estate tax law (R. 94). Like the Federal law, it contained a provision requiring the inclusion in the decedent's taxable estate of all

property over which the decedent had exercised a general power of appointment (§ 249-r, subd. 7). As originally enacted in 1930, however, Article 10-C did not purport to require the inclusion in the taxable estate of property, not otherwise a part of the decedent's estate, in respect of which the decedent had exercised only a special or limited power of appointment. This, again, followed the Federal law *which has never to this day contained any such provision.*

But in 1932 an amendment to Article 10-C was enacted adding a new subdivision, 7-a, to Section 249-r (L. 1932, c. 320), which, together with the introductory portion of Section 249-r, reads as follows:

> "§249-r. *Gross estate.* The value of the gross estate of the decedent shall be determined by including the value at the time of his death of all property, real or personal, tangible or intangible, wherever situated (except real property situated and tangible personal property having an actual situs outside this state):
>
> "1. To the extent of the interest therein of the decedent at the time of his death;
>
> * * * * * *
>
> "7-a. To the extent of any property passing under a power of appointment exercised by the decedent (a) by will, or (b) by deed executed in contemplation of, or intended to take effect in possession or enjoyment at or after, his death, except in case of a bona fide sale for an adequate and full consideration in money or money's worth, exclusive of property the value of which is required to be included in the gross estate pursuant to paragraph numbered seven of this section, and provided that the transfer of such property is not or was not subject to a death tax in the estate of the grantor of such

power but would have been so taxable except for a statute providing that the tax on the transfer of such property should be imposed in the estate of the grantee of such power in the event of the exercise thereof."

It is this 1932 amendment which has been held by the State Courts in this case to require the inclusion in the decedent's taxable estate of the trust fund above described (R. 96).

In order to consider this 1932 amendment in the light of the circumstances under which it was enacted, it is necessary that there be set forth a brief history of the previous treatment of powers of appointment for purposes of death taxation in the State of New York.

At the time of the death of Cornelius Vanderbilt, the grantor of the power, in 1899, the legacy tax law then in force in New York provided that all property subject to powers of appointment, whether the power was general or special, should be taxed upon the death of the grantee of the power, as though the property were received by the beneficiary from the grantee of the power, instead of from the grantor (§ 220, subd. 5, added by L. 1897, c. 284). By its terms, the statute required appointive property to be so taxed, *i.e.* in proceedings conducted in the estate of the grantee, whether or not the power was exercised. Subsequently, however, the statute was held unconstitutional in so far as it purported to make the legacy tax payable in the estate of the grantee of the power where the power was not exercised and the beneficiary received the property in default of appointment. *Matter of Lansing*, 182 N. Y. 238 (1905).

In conformity with this decision, the statute was amended in 1911 to provide for taxation in the estate

of the grantee of the power only in the event of exercise of the power; otherwise in the estate of the grantor of the power (§ 220, subd. 6, as amended by L. 1911, c. 732).

Even with this change, however, there was no provision for the case of a power exercised by the will of a grantee who was not a resident of the State of New York at the time of death. In such a case, no legacy tax at all would have been payable under the statute in respect of the property subject to the power: none in the grantor's estate, because the power had been exercised, and none in the grantee's estate, because the New York legacy tax law was not applicable to the estate of a non-resident grantee.

To meet this situation, the Legislature in 1926 provided that if the power should be exercised by the will of a grantee who was a non-resident of the State of New York at the time of death, the appointive property should be treated in the same way as if the power had not been exercised, *i.e.*, the legacy tax should be imposed in the estate of the grantor of the power (§ 220, subd. 4, as amended by L. 1926, c. 357).

A similar situation arose when Article 10-C was enacted repealing the legacy tax statute in respect of all persons dying after September 1, 1930, and substituting as to such persons the new estate tax law. The New York legacy tax statute thereby became inapplicable to the grantee of a power of appointment who died after September 1, 1930, even though such grantee was a resident of the State, and so no legacy tax in respect of the appointive property could be imposed in the estate of the grantee of the power in the event of exercise of the power by a resident grantee. The situ-

ation would seem to have called for treatment similar to that provided in 1926 with respect to the exercise of powers by non-residents, *viz.*, to provide that in each such case the property should be treated in the same way as if the power had not been exercised, *i.e.*, that the old legacy tax should be imposed in the estate of the grantor of the power.

Instead, however, of following this course, which would seem plainly indicated if adherence to a rational and consistent plan of taxation was desired, the Legislature chose to enact a unique and unprecedented statute, *i.e.*, the 1932 amendment above mentioned, singling out for special treatment a limited group of cases of property subject to powers of appointment, in which limited group the State Courts have held the property involved in the present case to be included.

There are no committee reports or published debates which throw any light on the reasons or motives of the Legislature in enacting this highly unusual statute. In 1930, when Article 10-C was enacted, the Legislature acted on the report of a specially appointed commission, known as the Commission to Investigate Defects in the Law of Estates, which had made a careful study of the subject. See *Matter of Cregan*, 275 N. Y. 337, 341 (1937). The 1932 amendment, however, was not recommended by this Commission, but was submitted to the Legislature as a so-called "Tax Department bill" (R. 52).

Tax Department bills "usually consist of ones which remedy discrepancies in the laws * * *. They are very seldom bills over which there would be any controversy" (R. 52). It is fair to assume, therefore, that the Tax Department bill which resulted in the 1932

amendment received only perfunctory attention in the Legislature and was passed on the assumption that it was of a minor administrative nature. There is no reason to suppose that the Legislature was aware that the bill represented a new departure in the field of estate taxation which had never before been attempted, either in the State of New York or by the Federal Government, whose system of estate taxation had previously been adopted by the State. Nor is there any reason to suppose that the Legislature was aware that the bill was inconsistent with the manner in which the Legislature had dealt with closely similar situations in 1911 and 1926.

All that has been found by way of explanation of the enactment of the 1932 amendment is a memorandum from Tax Department counsel to the President of the appellee Tax Commission, apparently written for the Governor after the bill had been passed, which reads as follows (R. 53):

"CHAPTER 320, LAWS 1932

Amending Section 249-r of the Tax Law by the addition of subdivision 7-a

"Under the inheritance tax laws in effect prior to September 1, 1930, where a person created a power of appointment, general, special or limited, provision was made that the property to which such power related should not be subject to death taxation in the estate of the grantor of the power in the event the power should be exercised, but should be taxable in the estate of the person exercising the power. Under the estate tax act in effect from 1925 to September 1, 1930, property transferred subject to general, special or limited powers of appointment

was subject to tax in the estate of the grantor of the power. The estate tax law which took effect on September 1, 1930 taxes the exercise of a general power of appointment, but does not tax the exercise of a special or limited power of appointment. For this reason, property now transferred by the exercise of a special or limited power of appointment created prior to September 1, 1930 may in some cases escape taxation in both the estate of the grantor and the estate of the grantee of the power. Equitably there should be one tax on property so transferred. This bill provides that property transferred by the exercise of a special or limited power of appointment shall be included in the decedent's gross estate for the purpose of the present estate tax in the event it is not taxable or has not been taxed in the estate of the grantor of the power and thus insures that one death tax will be imposed upon such property."

This memorandum ignores the fundamental differences between the considerations justifying, and the effect of, the old legacy tax and the new estate tax, and throws no light whatsoever on the reasons for not following what would seem to have been the plainly indicated course, *viz.*, to provide for the imposition of the old legacy tax in respect of such property in the estate of the grantor of the power, just as would be done either in the case of failure to exercise the power or in the case of exercise of the power by a non-resident decedent.

Not only is the 1932 amendment out of line with the general New York plan of taxation with reference to powers of appointment, but it is also inconsistent with the treatment of contingent remainders upon the shift in 1930 from a system of legacy taxation to a

system of estate taxation. At the time of the enactment of Article 10-C, there were many cases pending where persons had died at various times in the past leaving property subject to contingent remainders which had not yet fallen in, and where final determination of the legacy tax due under the old law had been postponed until the final destination of the legacy should be known, since the applicable rate of tax depended on consanguinity and on the total amount received from the particular decedent by any one recipient.

In the case of such contingent remainders, there was no attempt by the Legislature to impose the new estate tax in respect of any of the property subject to such contingent remainders. On the contrary, Article 10-C was so drawn as to continue the old legacy tax law in force as to such property (§ 249-mm, added by L. 1930, c. 710). That this effect was intentional is plainly shown by the enactment, together with Article 10-C, of an amendment of the legacy tax law providing for the immediate liquidation of the suspended legacy tax in such cases, at the option of the taxpayer, by the making of a compromise payment in the amount of the average of the highest and lowest legacy tax which could ultimately become due (§ 233, as amended by L. 1930, c. 711).

SPECIFICATIONS OF ERRORS TO BE URGED

The appellants intend to urge all of the errors described in their assignment of errors (R. 108).

SUMMARY OF ARGUMENT

I. The appellants' first contention is that the statute as applied in this case deprives them of their

property without due process of law in contravention of Section 1 of the Fourteenth Amendment to the Constitution of the United States.

II. The appellants' second contention is that, even if the statute here were applicable to all non-general powers of appointment whenever created, the imposition of the tax here in question would deprive the appellants of the equal protection of the laws, likewise in contravention of Section 1 of the Fourteenth Amendment to the Constitution of the United States.

III. The appellants' third and final contention is that the applicability of the statute only to non-general powers of appointment created before September 1, 1930, constitutes an additional and separate ground of invalidity under the equal protection clause of the Fourteenth Amendment.

POINT I

THE STATUTE AS APPLIED IN THE PRESENT CASE DEPRIVES THE APPELLANTS OF THEIR PROPERTY WITHOUT DUE PROCESS OF LAW.

An estate tax statute which requires the inclusion of property in the decedent's taxable estate merely because the decedent exercised a power of appointment over such property, constitutes an arbitrary and capricious allocation of the tax burden where, as in this case, the power of appointment is not a general power but only a limited power which the decedent was precluded from exercising for the benefit of herself, her creditors or her estate, and the property subject to the power is property which has never at any time belonged to the decedent.

In such a case, no justification for the tax can be found in a legislative purpose to prevent evasion or avoidance of the tax, such as justifies the inclusion in the taxable estate of property transferred in contemplation of death or to take effect at death, or any other property which once belonged to the decedent where the transaction, viewed as a whole, may fairly be regarded as a substitute for a testamentary disposition by the decedent. The tax in the present case could only be rested upon the assumption that the decedent stood in a relationship to the property here involved which was the practical equivalent of ownership, and on the undisputed facts of this case, as conclusively determined by the State Courts, this assumption is erroneous and arbitrary.

The appellants' contention does not rest upon any insistence on technical rules as to title—the recondite learning of ancient property law—or upon any claim that the Legislature is powerless to look through form to substance. The appellants recognize that substance, not form, must be regarded.

The appellants contend, however, that, giving full effect to substance rather than form, the treatment as part of the decedent's estate, for the purpose of measuring a progressive estate tax on the transmission of her estate, of property which the decedent never owned, either in a technical or a practical sense and either at death or at any previous time, necessarily involves an assumption of fact which is arbitrary and capricious and necessarily results in an allocation of the tax burden which is so devoid of any rational justification as to be contrary to the fundamental conceptions which underlie our form of government and are guaranteed by the due process clause.

a. **An estate tax cannot constitutionally be measured by property in which the decedent has never at any time had any beneficial interest.**

This Court is thoroughly familiar with the distinction between a legacy tax, which is a tax imposed on the right of a recipient to receive property on a death, and an estate tax, which is a tax imposed on the right of the decedent to transmit his property at death. See, for example, *Knowlton* v. *Moore,* 178 U. S. 41, 49, 77 (1900); *Y. M. C. A.* v. *Davis,* 264 U. S. 47, 50 (1924); *Edwards* v. *Slocum,* 264 U. S. 61, 62-3 (1924).

(1) *There may properly be included in the measure of an estate tax property not technically owned by the decedent at death if the decedent stood in a relationship to the property which might fairly be regarded as the equivalent of ownership.*

It follows from the very nature of an estate tax that basically the tax must be measured by the property owned by the decedent and transmitted to his heirs and legatees upon his death. This does not mean, however, that the decedent must have owned property in a technical title sense in order for it to be proper to include it in the measure of an estate tax. It is sufficient that the decedent stood in a relationship to the property which, as a practical matter, might fairly be regarded as the equivalent of ownership.

Thus, the inclusion in the measure of the tax of property in respect of which the decedent exercised a general power of appointment is valid although in a technical sense property subject to such a power is not owned by the grantee of the power. *Bullen* v. *Wisconsin,* 240 U. S. 625 (1916). But, as has been pointed out

by Circuit Judge Parker in *Leser* v. *Burnet*, 46 F. (2d) 756 (C. C. A. 4th, 1931), this is true only because a general power of appointment gives the grantee of the power the substantial equivalent of ownership, since he is free to exercise the power in favor of his creditors and thus use the property for his own benefit.

In the *Leser* case, which involved the question whether the decedent had exercised a general power of appointment within the meaning of the Federal estate tax law, the power was general on its face, but under the applicable Maryland law, a grantee of a power of appointment had no right to appoint to his own creditors unless this right was specifically granted, which had not been done in the case at issue. In holding that the appointed property should be excluded from the grantee's taxable estate, the Court, through Judge Parker, said (pp. 759-60):

> "Except that the donee of a general power may exercise it in favor of his creditors and thus use the property which is the subject of the power for his own use and benefit, there is no basis for including in his taxable estate property which is subject thereto; for this right is all that passes from his estate by reason of his death. * * * Nothing passes or is transferred from the estate of the donee in the case of a naked or special power of appointment, and Congress has recognized this fact by not requiring that property passing under a special power be included in the estate. It is only property subject to a general power—property of which the donee might have obtained the benefit by subjecting it to the payment of his debts—which is required to be included.
>
> * * * * * * *

> "It thus appears that the purpose of Congress was to tax property in relation to which the donee of a power stands in a position not unlike that of owner, property over which he exercises the same authority as he does over that which he owns. This could be said of property which he could subject to the payment of his debts. It could not be said of a naked power which he could not exercise for his own benefit or for the benefit of his estate."

To the same effect, see also *Fidelity-Philadelphia Trust Co.* v. *McCaughn,* 34 F. (2d) 600, 604 (C. C. A. 3d, 1929), cert. denied 280 U. S. 602; *cf. Morgan* v. *Commissioner,* U. S. Sup. Ct., Oct. Term, 1939, No. 210, decided Jan. 29, 1940.

Another instance of the inclusion in the measure of an estate tax of property not technically owned by the decedent because the decedent in a practical sense had the substantial equivalent of ownership, is the case of the proceeds of insurance policies taken out by the decedent on his own life. If the decedent at death retains the power to change the beneficiary, surrender the policy and borrow on it, it is proper to require the proceeds of the policy to be included in the decedent's taxable estate for the purpose of an estate tax. *Chase National Bank* v. *United States,* 278 U. S. 327 (1929).

It should be noted, however, that although the insurance provisions of the Federal estate tax law * would seem on their face to require the inclusion of the

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* Revenue Act of 1926, §302-g, reading as follows:

> "To the extent of the amount receivable by the executor as insurance under policies taken out by the decedent upon his own life; and to the extent of the excess over $40,000 of the amount receivable by all other beneficiaries as insurance under policies taken out by the decedent upon his own life."

proceeds of *all* insurance policies taken out by the decedent on his own life (subject only to a $40,000 exemption in the case of policies payable to a beneficiary other than the decedent's executor), the statute has consistently been held *not* to require the inclusion of the proceeds of any policy in which the decedent at death had no beneficial interest. *Helvering* v. *Parker*, 84 F. (2d) 838 (C. C. A. 8th, 1936); *Pennsylvania Co.* v. *Commissioner*, 79 F. (2d) 295 (C. C. A. 3d, 1935), cert. denied 296 U. S. 651; *Levy's Estate* v. *Commissioner*, 65 F. (2d) 412 (C. C. A. 2d, 1933); *McKelvy* v. *Commissioner*, 82 F. (2d) 395 (C. C. A. 3d, 1936); *Ballard* v. *Helburn*, 9 F. Supp. 812, affd. 85 F. (2d) 613 (C. C. A. 6th, 1936). These decisions, which are entirely consistent with the earlier *Chase National Bank* case, have been accepted by the Treasury Department and their holding has been incorporated in its regulations (T. D. 4729, approved March 18, 1937; Reg. 80, Art. 25).

(2) *The necessity of preventing evasion or avoidance of the tax permits the inclusion of property once owned by the decedent in various types of cases where the transaction as a whole may fairly be regarded as a substitute for a testamentary disposition.*

The measure of an estate tax may properly include property which at death the decedent did not own in any sense, technical or practical, if the statutory provision requiring the inclusion of such property is reasonably appropriate to a legislative purpose to prevent evasion or avoidance of the tax.

It is this principle which permits the inclusion in the decedent's taxable estate of property which the decedent at death no longer owns but which he has

previously transferred in contemplation of death or to take effect at or after death. *United States* v. *Wells*, 283 U. S. 102 (1931). In that case, involving the Federal estate tax law, this Court, through Mr. Chief Justice Hughes, said (pp. 116-17):

> "The quality which brings the transfer within the statute is indicated by the context and manifest purpose. Transfers in contemplation of death are included within the same category, for the purpose of taxation, with transfers intended to take effect at or after the death of the transferor. The dominant purpose is to reach substitutes for testamentary dispositions and thus to prevent the evasion of the estate tax."

This same principle justifies the inclusion of property in the measure of an estate tax in a variety of situations where the property had once belonged to the decedent and the transaction viewed as a whole, may fairly be regarded as the equivalent of a testamentary disposition by the decedent. Examples of such situations are: *Reinecke* v. *Northern Trust Co.*, 278 U. S. 339 (1929), where the decedent during his lifetime had transferred the property in trust but had retained until his death a right to revoke the trust; *Helvering* v. *City Bank Co.*, 296 U. S. 85 (1935), where a right of revocation in conjunction with one of the beneficiaries had been retained by the decedent; *Porter* v. *Commissioner*, 288 U. S. 436 (1933), where the decedent had retained control of the disposition of the property until his death through the reservation to himself of a power to modify the trust except in his own favor; *Tyler* v. *United States*, 281 U. S. 497 (1930), where the decedent had placed his property in a

tenancy by the entirety; and *United States* v. *Jacobs*, 306 U. S. 363 (1939), where the decedent had placed his property in a joint tenancy.

In all such cases, the decedent had once been the owner of the property and had utilized some device which in substance accomplished a testamentary disposition by the decedent of his own property notwithstanding that in form the decedent had divested himself of the property prior to his death. In such cases, it is often a close question whether the statutory provision in question, requiring the inclusion of the property in the decedent's taxable estate, falls on one side or the other of the line of measures reasonably appropriate to the legislative purpose to prevent evasion or avoidance of the estate tax. Thus, in *Helvering* v. *City Bank Co.*, 296 U. S. 85 (1935), cited above, the Court said (p. 90):

> "A legislative declaration that a status of the taxpayer's creation shall, in the application of the tax, be deemed the equivalent of another status falling normally within the scope of the taxing power, *if reasonably requisite to prevent evasion*, does not take property without due process. But if the means are unnecessary or inappropriate to the proposed end, are unreasonably harsh or oppressive, when viewed in the light of the expected benefit, or arbitrarily ignore recognized rights to enjoy or to convey individual property, the guarantee of due process is infringed." (Italics supplied.)

Cf. Helvering v. *Helmholz*, 296 U. S. 93 (1935); *Helvering* v. *Hallock*, U. S. Sup. Ct., Oct. Term, 1939, Nos. 110, 111, 112, 183, and 399, decided Jan. 29, 1940.

Where, however, the property in question has *never* belonged to the decedent, a requirement that the prop-

erty be included in his taxable estate for purposes of an estate tax cannot in any case be justified on the basis of a legislative purpose to prevent evasion or avoidance of the estate tax. The question whether a particular measure is reasonable or appropriate to such a legislative purpose does not arise, because, if the decedent has *never* owned the property, the legislative purpose cannot possibly have been to prevent him from evading or avoiding an estate tax on his estate by the use of some device which would in substance accomplish a testamentary disposition by him of his property. In such a case, there is wholly lacking the basic foundation for the principle here under consideration.

(3) *Where the decedent has never had any beneficial interest in the property in question, either at death or at any previous time, the inclusion of the property in the decedent's taxable estate for purposes of an estate tax is contrary to due process of law.*

In such a case, the tax can be based only upon an arbitrary assumption which is unfounded in fact, and it is well settled that a tax resting upon an arbitrary and erroneous factual assumption constitutes a denial of due process of law. *Heiner* v. *Donnan*, 285 U. S. 312 (1932); *Hoeper* v. *Tax Commission*, 284 U. S. 206 (1931); *Schlesinger* v. *Wisconsin*, 270 U. S. 230 (1926); *Nichols* v. *Coolidge*, 274 U. S. 531 (1927); *Frew* v. *Bowers*, 12 F. (2d) 625 (C. C. A. 2d, 1926).

The *Donnan* case above cited involved the validity, under the due process clause, of a provision in the Federal estate tax law to the effect that a transfer of property made by the decedent within two years prior

to his death should be "deemed and held to have been made in contemplation of death". The Court held this provision invalid as a denial of due process of law, saying (285 U. S. 327):

> "The result is that upon those who succeed to the decedent's estate there is imposed the burden of a tax, measured in part by property which comprises no portion of the estate, to which the estate is in no way related, and from which the estate derives no benefit of any description. Plainly, this is to measure the tax on A's property by imputing to it in part the value of the property of B, a result which both the *Schlesinger* and *Hoeper* cases condemn as arbitrary and a denial of due process of law. Such an exaction is not taxation but spoliation."

The *Schlesinger* case involved the validity, under the due process clause, of a similar conclusive presumption in a legacy tax law of the State of Wisconsin, the period in this case, however, being six years instead of two.

In the *Hoeper* case, the Court held invalid, under the due process clause, a provision of an income tax law of the State of Wisconsin to the effect that the income of a husband should be deemed to include the income of his wife. In so holding, the Court, through Mr. Justice Roberts, said (284 U. S. 215):

> "We have no doubt that, because of the fundamental conceptions which underlie our system, any attempt by a state to measure the tax on one person's property or income by reference to the property or income of another is contrary to due process of law as guaranteed by the Fourteenth Amendment. That which is not in fact the taxpayer's income cannot be made

such by calling it income. Compare *Nichols* v. *Coolidge*, 274 U. S. 531, 540."

While the *Donnan*, *Schlesinger* and *Hoeper* cases were each decided by a divided Court, none of the Justices of this Court who dissented in these cases questioned the soundness of the principle for which these cases are cited; they merely took the position that, in these instances, the principle was inapplicable. Mr. Justice Stone disagreed with the decision in the *Donnan* case on the ground that the conclusive presumption provision could be sustained as imposing a gift tax designed to prevent evasion or avoidance of the estate tax (see 285 U. S. at pp. 335, 338 *et seq.*). Similarly, in the *Schlesinger* case, Mr. Justice Holmes rested his dissent on the ground that the conclusive presumption provision might reasonably have been thought necessary to prevent evasion or avoidance of the estate tax (see 270 U. S. at p. 242). And in the *Hoeper* case, Mr. Justice Holmes argued for the validity of the tax on the ground that a husband might reasonably be thought to derive a benefit in fact from his wife's income (see 284 U. S. at pp. 219-20).

Certainly this Court has never held, or even suggested, so far as has been discovered, that property which the decedent had never owned might properly be included in his taxable estate for purposes of an estate tax, merely because he exercised a limited and non-beneficial power of appointment over such property.

It is clear that those responsible for Federal tax legislation have not believed that an estate tax law could validly require the inclusion of such property. Notwithstanding that the Federal estate tax law

has for many years, ever since the Revenue Act of 1918, required the inclusion in the decedent's taxable estate of property passing under a general power of appointment exercised by the decedent, there never has been any attempt to require the inclusion of property in respect of which the decedent has exercised only a limited and non-beneficial power. If it were believed that such a requirement would be valid, it hardly seems likely that any such source of additional revenue by the estate tax method would have been overlooked.

It is likewise significant that when the New York estate tax law was enacted in 1930, on the recommendation of a learned commission which had made a careful study of the subject (see p. 9 above), no such provision was inserted in the new law, either. It was not until the enactment of the 1932 amendment, which is involved in the present case, that any attempt was made to require the inclusion of such property in the measure of the tax, and then only in the restricted group of cases to which such amendment by its terms is limited.

Since there has been no previous attempt to require the inclusion in the measure of an estate tax of property in which the decedent had never had any beneficial interest either at death or at any previous time, it is of course impossible to cite any decision in which it was specifically held that such a requirement constitutes a denial of due process of law. It is believed, however, that this result necessarily follows from the other decisions to which reference has been made above.

b. The decedent in the present case has never at any time had any beneficial interest in the property here involved.

The property here involved is the remainder interest in the trust created by the will of Cornelius Vanderbilt. The only connection of the decedent with such property is that she had and exercised a limited power of appointment over such property of a kind which, under the applicable State law, constituted a special power in trust giving the decedent no beneficial interest whatsoever in such property. A determination to this effect on this question of State law has been made by the New York Court of Appeals in this case, in the following language (R. 87-8):

> "*The property* which was included in Mrs. Vanderbilt's estate (*i.e.*, the appointed property here in question) *did not at any time belong to her.* It did not at her death pass from her to those whom she appointed to take. Her power of appointment was not general. *By its exercise she could obtain no benefit for herself, her creditors or her estate.* During her life the fund was held by trustees under the terms of the will of Cornelius Vanderbilt. She enjoyed under his will a life interest in the fund, and a tax measured by the value of that life interest was paid upon the death of Cornelius Vanderbilt. The remainder, which would vest in others upon her death, was not included in the tax assessed upon the transfer of his property. Mrs. Vanderbilt might, by exercise of her power of appointment, determine the shares which members of a limited group defined by the will of Cornelius Vanderbilt should receive out of property in the estate of Cornelius Vanderbilt and held by trustees under his will. *When she exercised*

that power she gave her appointees nothing which belonged to her and she relinquished no rights which she might have asserted for herself." (Parenthetical clause and italics supplied.)

On familiar principles, this determination by the highest Court of the State on this question of State law is conclusive.

It is clear that in stating that the property here involved "did not at any time belong to" the decedent, the Court of Appeals is not referring merely to ownership in a technical sense. The remainder of the quoted excerpt and various other passages in the opinion make it clear that the Court's determination is that the decedent did not at any time have any beneficial interest in the property.

It is true that in reaching its conclusion that the "unfairness" of the tax here imposed was not such as to render the statute invalid (R. 99), the Court speaks of a "practical transfer" (R. 97) of this property by the decedent, and states that this property "was in a practical sense transferred by the will of the grantee of the power" (R. 97-8). These statements will be discussed further below, under a subsequent subdivision of this Point I. But it should here be noted that in making these statements, the Court is not in any way suggesting that this property belonged to the decedent, even in a practical sense; on the contrary, the Court clearly recognizes that this property which, it says, was "in a practical sense" transferred by the will of the decedent, was the property of some one else, not of the decedent (see R. 98-9).

Consequently, if it is true, as the appellants contend, that the due process clause does not permit the

inclusion in the measure of an estate tax of property in which the decedent had never had any beneficial interest, either at death or at any previous time, the conclusion seems inescapable that the statute here in question, as applied in the present case, cannot be sustained.

c. **The fact that upon the death of this decedent a legacy tax might have been imposed upon the receipt of this property by the appointees does not justify the tax here in question.**

The appellants concede that if we were here dealing with a legacy tax on the receipt by the appointees of the property here involved, measured by the amount received by the appointees respectively, none of the appointees could complain of the Legislature's selection of the exercise of the power by the grantee as the occasion for the imposition of the tax on his undoubted receipt, at that time, of the property appointed to him. Such is the holding of *Orr* v. *Gilman,* 183 U. S. 278 (1902), affirming *Matter of Dows,* 167 N. Y. 227 (1901), and *Chanler* v. *Kelsey,* 205 U. S. 466 (1907), affirming *Matter of Delano,* 176 N. Y. 486 (1903).

Since the gift is incomplete, so far as the appointee is concerned, until the power has been exercised by the grantee, a tax on his receipt of the property is not retroactive if enacted before the exercise of the power. Thus, in *Chanler* v. *Kelsey,* cited above, the Court said (205 U. S., at pp. 473-4):

> "However technically correct it may be to say that the estate came from the donor and not from the donee of the power, it is self-evident that it was only upon the exercise of the power that the estate in the plaintiffs in error [the appointees] became complete."

But the appellants have never taken, and do not now take, the position that the tax here in question is invalid because it was too late, when the statute here was enacted, to impose *any* tax. Their position is simply that the tax which was actually imposed is so arbitrary and so inconsistent with any rational plan of taxation, that it cannot stand under the due process clause.

This Court has repeatedly pointed out, in effect, that the question whether a legacy tax may be validly imposed under particular circumstances is a wholly different question from the question whether an estate tax may be validly imposed under the same circumstances. See, for example: *Nichols* v. *Coolidge*, 274 U. S. 531, 541 (1927); *Saltonstall* v. *Saltonstall*, 276 U. S. 260, 270-1 (1928); *Coolidge* v. *Long*, 282 U. S. 582, 608, 609, 631-2 (1931); *cf. Knowlton* v. *Moore*, 178 U. S. 41, 49, 77 (1900); *Y. M. C. A.* v. *Davis*, 264 U. S. 47, 50 (1924); *Edwards* v. *Slocum*, 264 U. S. 61, 62-3 (1924).

The significance attributed to this distinction by Justices of this Court is strikingly shown by the cases of *Nichols* v. *Coolidge* and *Coolidge* v. *Long*, cited above, which involved, respectively, a Federal estate tax and a Massachusetts legacy tax in respect of precisely the same property. In both cases the tax was held invalid, but in the *Nichols* case, involving an estate tax, Justices Holmes, Brandeis, Stone and Sanford concurred in the result, whereas in the *Long* case, involving a legacy tax, Justices Holmes, Brandeis and Stone joined with Mr. Justice Roberts in dissenting from the decision. The dissenting opinion in the *Long* case expressly distinguished the *Nichols* case on the

ground that the *Nichols* case involved an estate tax rather than a legacy tax (see 282 U. S. at 609, 622-3).

Where a legacy tax is being imposed on the exercise of a power of appointment, it is immaterial whether the grantee of the power had, or had ever had, any beneficial interest in the property subject to the power. The tax is imposed on the receipt of the property by the appointee and is measured by the property which the appointee receives. There is no question but that the appointee does in fact receive the property by which the tax is measured. There is also no question but that he does not in fact receive it until the power has been exercised. The imposition of the tax at the time of the exercise of the power, instead of at the time of the death of the grantor of the power, may result in the application of higher rates where, as is sometimes the case, the rates have been increased between the time of the death of the grantor of the power and the time of the exercise of the power. But where the tax is on the receipt of property, the application of rates in force at the time when the property is actually received cannot be regarded as arbitrary, and may even be thought to be more fair than the application of earlier rates.

Where, however, it is sought to impose an *estate* tax upon the exercise of a power of appointment, the question whether the grantee of the power had, or had ever had, any beneficial interest in the property subject to the power, is of controlling importance. Since the tax is imposed on the transmission of the grantee's estate, and is measured by the total amount of that estate, to whomsoever and in what proportions it may be transmitted, the treatment of the appointed property as part of the grantee's estate for the purpose of

measuring the tax is wholly arbitrary where there is no basis in fact for so regarding the property. Where, as in the present case, the grantee of the power had never owned the appointed property (so that the principle of preventing evasion or avoidance is inapplicable), and the power is a special power in trust which the grantee was precluded from exercising for the benefit of herself, her creditors or her estate (so that there is no basis for an assumption that the grantee stood in a relation to the property which was the practical equivalent of ownership), there is no rational justification whatsoever for an estate tax measured by treating the appointed property as part of the grantee's estate.

The difference between the two situations, *i.e.*, the imposition of a legacy tax upon the receipt of appointed property upon the exercise of a non-beneficial power and the inclusion of such property in the taxable estate of the grantee for purposes of an estate tax, is not a mere matter of legal theory, of no practical consequence, but is a matter of real substance. That this is so is well shown by the facts of the present case.

If in this case a legacy tax had been imposed in respect of the appointed property, and if the taxing statute had prescribed a progressive scale of rates identical with the rate scale prescribed in the actual estate tax law here in question, the legacy tax would be measured in the case of each appointee by the property appointed to such appointee (together with any other property received by the appointee from this decedent), and the applicable rates in the progressive scale would be determined accordingly. The estate tax, on the other hand, is measured not by the property appointed to any one appointee, nor even by the aggregate of all of the property appointed to all of the ap-

pointees, but by the aggregate of all of the appointed property and all of the decedent's own property. Such aggregation results in the application of substantially higher rates in the progressive rate scale. By reason of such aggregation, the portion of the estate tax imposed in the present case which corresponds in ratio to the total amount of the appointed property included in the decedent's taxable estate (about $685,000), is approximately $315,000 in excess of the total legacy tax which would have been imposed in respect of such property under a legacy tax statute containing an identical scale of progressive rates.

Furthermore, the balance of the estate tax imposed in this case, *i. e.*, the portion (about $525,000) corresponding in ratio to the total amount of the decedent's own property, is approximately $165,000 in excess of the total estate tax (about $360,000) which would have been payable in this case under the statute here in question if a legacy tax had been imposed in respect of the appointed property instead of treating such property as part of the decedent's taxable estate for the purpose of this estate tax (*cf.* R. 67).

These consequences of the imposition here of an estate tax in respect of the appointed property, instead of a legacy tax, are not set forth as supplying any reason in themselves for invalidating the tax. If there were some rational justification for treating the appointed property as part of the decedent's taxable estate, those who bear the burden of the tax in respect of the decedent's own property could not complain of the increase in their tax burden resulting from the aggregation of which mention has been made. But where, as here, the aggregation rests upon an erroneous and arbitrary assumption of fact, it becomes rele-

vant to inquire whether the resulting differences in tax burden are trivial or substantial. The illustrations given sufficiently show, it is believed, that these differences are substantial.

It is no answer to say that a State has discretion, within very broad limits, as to the rate of tax, and that the difference in consequences between the estate tax here involved and a legacy tax is no more disadvantageous to those bearing the burden of the tax than would be an increase in the rate. This Court has squarely held that a State may not include in the measure of a death tax property in respect of which it had no power to impose the tax in question even though the effect of such inclusion is no different than would be a tax at a higher rate measured solely by property in respect of which the State did have power to impose the tax. *Frick* v. *Pennsylvania*, 268 U. S. 473 (1925).

d. **No adequate ground for sustaining the tax here in question can be found in the opinion of the New York Court of Appeals.**

The New York Court of Appeals recognizes that we are here dealing with an estate tax which must be distinguished from a legacy tax, and that the differences between a legacy tax and an estate tax "are not merely theoretical" (R. 93-4).

Nevertheless, the Court's ultimate conclusion that the estate tax here in question "is not so unreasonable that it may be challenged in the courts" (R. 99), is fundamentally based upon the decisions already discussed above (pp. 27 *et seq.*) sustaining the imposition of a legacy tax in respect of property appointed under a non-beneficial power at the time of the exercise of such power. The Court twice quotes from its own opinion in one of these decisions, *Matter of Delano*,

176 N. Y. 486, 494, a statement that in the case of such a tax, "it is the practical transfer through the exercise of the power by will that is taxed and nothing else" (R. 92, 97). It is this statement which is the source of the statements in the present opinion to which reference has been made above (p. 26) to the effect that there was a "practical transfer" of the appointed property here when the decedent exercised the power by her will (R. 97-8).

From this, the Court reasons that the "Legislature was free at that time to impose a tax upon such transfer" (R. 97). And up to this point, as has already appeared, there is no divergence between the views expressed by the Court of Appeals and the position taken by the appellants.

Thereupon, however, the Court takes the next step, although not without some obvious difficulty, *viz.*, that when the Legislature chose to impose an estate tax, "measured by the aggregate of the property transferred under her will" (R. 99), "even though the decedent did not own some of the property but merely had a limited power of appointment" (R. 98), this was not "entirely without basis in fact" (R. 98), and while "argument can be made that such a tax is not fair" (R. 98), such "'unfairness' does not, however, render the statute invalid" (R. 99).

Heiner v. *Donnan*, 285 U. S. 312 (1932), cited above, is distinguished by the Court of Appeals on the ground that in the *Donnan* case, "by arbitrary choice to include in the 'estate' of the decedent property which did not pass at the decedent's death to which the estate was in no way related and from which the estate derived no benefit, the Legislature increased the rate of taxation upon the transfer of property which the de-

cedent owned and transmitted," whereas in the present case, "no property is included in the aggregate which measured the tax which does not pass at Mrs. Vanderbilt's death to persons who take the property only because she so provided in her will" (R. 98).

With all respect, it is submitted that this reasoning cannot be considered as supplying a satisfactory ground for sustaining the tax here in question. It fails to take account of the fact that in exercising the special power in trust granted to her in the will of her husband, the decedent was merely acting as her husband's fiduciary agent in connection with the disposition of *his* property. The circumstance that the decedent performed her fiduciary function with reference to her husband's property by means of the same instrument by which she disposed of her own property, surely cannot be regarded as a sufficient basis for including her husband's property in the measure of a tax on the transmission of the decedent's estate. So to regard this circumstance would seem wholly inconsistent, not only with the nature of the tax with which we are dealing, but also with the principle, so firmly established in this Court, that in considering the validity of a taxing statute, substance, not form, must be given effect.

From the standpoint of a tax on the receipt by each appointee of his share of the appointed property, the act of the decedent in exercising the power may, with some justification perhaps, be termed a "practical transfer" of the property to the appointees, since the property would have been received in different proportions by the appointees if the decedent had exercised the power differently or not at all. But from the standpoint of an estate tax on the transmission of

the decedent's estate, the proportions in which the appointees receive appointed property which never belonged to the decedent is a wholly immaterial circumstance. The measure of an estate tax does not depend upon the persons by whom the estate is received nor upon the proportions in which they receive it. Whatever justification there may be for regarding the exercise of the power in the present case as a "practical transfer" *to the appointees,* there is no justification whatever for regarding it as a "practical transfer", or any other kind of a transfer, *from the decedent.* As the Court of Appeals itself says, the property involved "did not at any time belong to her" (R. 87); when she exercised the power, "she gave her appointees nothing which belonged to her" (R. 88). From the standpoint of an estate tax on the transmission of the decedent's estate, only transfers *from the decedent* are significant (*cf.* Mr. Justice Stone, for the Court, in *Reinecke* v. *Northern Trust Co.*, 278 U. S. 339 (1929) at p. 348).

Accepting as authoritative the test laid down in the *Donnan* case (as quoted above at p. 22) as the Court of Appeals purports to do (R. 98) it seems utterly impossible to sustain the tax imposed in the present case. At least as clearly as in the *Donnan* case, the tax here has been "measured in part by property which comprises no portion of the estate, to which the estate is in no way related, and from which the estate derives no benefit of any description" (285 U. S. 327). Indeed, in the *Donnan* case, the property involved had admittedly been the property of the decedent not long before his death; in the present case, the property involved had never at any time been the property of the deceased.

The conclusion that the statute here in question is incompatible with the freedom from capricious official action which is guaranteed by the due process clause, is strongly re-enforced by the circumstances under which the enactment of the statute, *i.e.*, the 1932 amendment, was brought about. These circumstances are outlined in the introductory portion of this brief (pp. 7-12) and they indicate that the unusual nature and oppressive effect of the statute were not brought to the attention of either the Legislature or the Governor. Such circumstances go a long way in themselves toward rebutting the presumption of validity to which every statute is entitled when its constitutionality is under consideration in this Court. Furthermore, the explanation of the reasons for the statute which has been given by the administrative agency with which it originated (see memorandum set forth above, pp. 10-11), tends strongly to confirm the view that the statute, as applied in the present case, is so devoid of rational justification as to be plainly inconsistent with due process of law.

POINT II

EVEN IF THE STATUTE WERE APPLICABLE TO ALL NON-GENERAL POWERS OF APPOINTMENT WHENEVER CREATED, THE IMPOSITION OF THE TAX HERE IN QUESTION WOULD DEPRIVE THE APPELLANTS OF THE EQUAL PROTECTION OF THE LAWS.

The appellants complain not only of the failure to follow due rational process in imposing the tax in question, but also of the discriminatory result of such failure. Under Point I, attention was directed to the lack of rational method condemned by the due process clause; under this Point II, there will be noted the unreasonable discrimination thereby brought about.

a. **The equal protection clause imposes a more exacting requirement of fairness than does the due process clause.**

The equal protection clause has no counterpart in the Fifth Amendment and is, therefore, inapplicable to Federal action. A state statute, however, must be consistent both with the due process clause and with the equal protection clause. The same state statute may infringe both clauses. However, a state statute which is not so arbitrary as to be condemned by the due process clause may, nevertheless, be sufficiently oppressive or unequal in effect as to fail to conform with the more stringent standard to which the States are bound by the equal protection clause.

As was said by Chief Justice Taft, for the Court, in *Truax* v. *Corrigan*, 257 U. S. 312 (1921), where it was held that the equal protection clause forbade withdrawal of certain equitable remedies even if the due process clause allowed it (pp. 331-2):

> "The [equal protection] clause is associated in the Amendment with the due process clause and it is customary to consider them together. *It may be that they overlap, that a violation of one may involve at times the violation of the other, but the spheres of the protection they offer are not coterminous.* * * * The due process clause * * *, of course, tends to secure equality of law in the sense that it makes a required minimum of protection for every one's right of life, liberty and property, which the Congress or the legislature may not withhold. * * * But the framers and adopters of this Amendment were not content to depend on a mere minimum secured by the due process

clause, or upon the spirit of equality which might not be insisted on by local public opinion. They therefore embodied that spirit in a specific guaranty.

"The guaranty was aimed at undue favor and individual or class privilege, on the one hand, and at hostile discrimination *or the oppression of inequality*, on the other. It sought an equality of treatment of all persons, even though all enjoyed the protection of due process. * * *" (Italics supplied.)

See also *LaBelle Iron Works* v. *United States*, 256 U. S. 377, 392 (1924); *Heiner* v. *Donnan*, 285 U. S. 312, 338, 347-8 (1932) (dissenting opinion).

b. The statute here discriminates between the estates of decedents who have exercised non-beneficial powers of appointment and those who have not.

The amount of property which the appellants concede to have been properly included in the decedent's gross estate, was $4,835,335.10 (R. 15). The amount of permissible deductions was $766,319.32, leaving a net taxable estate of $4,069,015.78 if the appointed property be excluded from the gross estate. The tax payable in respect of a net estate of that amount would be $360,207.55, the highest applicable tax bracket being the 13% bracket.

Because the appointed property was included in the gross estate (except for the $650,000 mentioned above at p. 3) the gross estate has been computed at $10,120,907.17. The amount of permissible deductions being $766,319.32, the net taxable estate has been held to be $9,354,587.85 (R. 8). A tax of $1,212,509.69 has been assessed and paid, the highest applicable tax bracket being the 19% bracket (R. 8).

Thus, an estate precisely like that of the decedent, so far as any property in which the decedent had ever had any beneficial interest is concerned, would be required to pay only $360,000 in estate tax, whereas the decedent's estate has been required to pay $1,212,000, a difference of $852,000.

The Court of Appeals in this case assumes (R. 98), without deciding, that there would be applicable here a provision of the Decedent Estate Law of the State of New York (Cons. Laws, c. 13, § 124) to the effect that the estate tax shall be prorated among the persons to whom the property in the estate is transferred, in the proportions that the value of the property received by each such person bears to the total value of the property received by all persons interested in the estate. If this assumption is correct, about $685,000 of the total estate tax exacted from the decedent's estate, *i.e.*, the proportion corresponding in ratio to the value of the appointed property, would ultimately be borne by the recipients of the appointed property.

Even on this assumption, however, those who succeed to the decedent's own property (who are represented in this case by the appellant executors) will have been required to pay a tax of about $165,000 more than would have been payable if the appointed property had not been included in the decedent's gross estate. Such is the effect of the aggregation of the appointed property with the decedent's own property and the consequent application of higher rates in the progressive rate scale, to which reference has already been made (pp. 30-1).

In other words, the State Courts have held that because the decedent has carried out a trust from which

no benefit could have been obtained for herself, her creditors or her estate, the persons who succeed to the decedent's property must pay some $165,000 more than other persons in precisely the same situation, save only that, in the one case, such a fiduciary function has been performed by the decedent, and in the other case it has not. Indeed, another decedent might even have exercised a power precisely similar except that it was exercisable either by will or by *inter vivos* deed, and if the exercise was by *inter vivos* deed, no tax would have been imposed in respect of the appointed property, either under the statute here in question or under any other statute of the State of New York.

c. There is no reasonable basis of classification which justifies the difference in treatment.

The various considerations to which attention has been directed by the appellants in connection with the due process question bear also, and with even greater force, upon the question whether the legislative classification satisfies the more exacting requirement of fairness imposed by the equal protection clause. Just as there is no conceivable factual premise upon which to justify the imposition of an estate tax in a situation such as the present one, so there is no conceivable reason why the Legislature should impose such a tax here while imposing no such tax in the similar case of a decedent owning the same amount of property who does not have the right to exercise a non-beneficial power of appointment, or refrains from exercising it, or has the right to exercise it by *inter vivos* deed and does so.

The usual statement of the requirement of the equal protection clause, as applied to State taxing statutes,

is that classification for the purposes of a State taxing statute must be reasonable, not arbitrary or capricious, and must rest upon some ground of difference having a fair and substantial relation to the object of the legislation. See, for example, *Royster Guano Co.* v. *Virginia*, 253 U. S. 412, 415 (1920); *Louisville Gas Co.* v. *Coleman*, 277 U. S. 32, 37 (1928).

A State Legislature has broad discretion as to classification for purposes of taxation and is not required "to adopt an iron rule of equal taxation" (*Madden, Jr.* v. *Kentucky*, U. S. Sup. Ct., Oct. Term 1939, No. 92, decided Jan. 29, 1940). It is clear, however, that the power is not unlimited, and that where, as here, it is shown that the statute is oppressive and discriminatory and rests upon an arbitrary and erroneous assumption of fact, it will not be permitted to stand. *Air-Way Electric Appliance Corporation* v. *Day*, 266 U. S. 71 (1924); *Smith* v. *Cahoon*, 283 U. S. 553 (1931); *Iowa-Des Moines National Bank* v. *Bennett*, 284 U. S. 239 (1931). In the present case, where it plainly appears from the circumstances under which the statute was enacted, as outlined in the introductory portion of this brief (pp. 9-11 above), that the classification was not occasioned by local conditions known to the Legislature, there is no room for the operation of any presumption based upon the Legislature's greater knowledge of local conditions.

The Court will not indulge pure conjecture in order to hypothesize a state of facts which might justify the discrimination. Thus, in *Gulf, Colorado and Santa Fe Ry. Co.* v. *Ellis*, 165 U. S. 150 (1897), the Court said (p. 154):

> "While good faith and a knowledge of existing conditions on the part of a legislature is to

> be presumed, yet to carry that presumption to the extent of always holding that there must be some undisclosed and unknown reason for subjecting certain individuals or corporations to hostile and discriminating legislation is to make the protecting clauses of the Fourteenth Amendment a mere rope of sand, in no manner restraining state action."

Similarly, in *Binney v. Long*, 299 U. S. 280 (1936), discussed at length under Point III below, the Court said (p. 294):

> "While this court always accords great weight to the judgment of a state legislature, we cannot agree that there is here a fair basis for difference of treatment. All that is said in defense of the statute is that it treats alike all those who take under instruments executed prior to an arbitrary past date, and treats alike all those who take under instruments made subsequently to the same arbitrary date, and that the legislature may have found some reason for the discrimination in the state's policy of taxation. But this is merely to say that arbitrary classification which is the result of the exercise of the legislative will must be sustained."

In the present case, the only suggestion as to a possible reason of policy justifying the discrimination of which complaint is here made, is that the 1932 amendment of the estate tax law was required to prevent the escape of the property here involved from all death taxation through the inadvertent repeal, by the new estate tax law, of the old legacy tax which would have been payable upon the exercise, after the effective date of the new estate tax law, of powers theretofore created. See memorandum of Tax Department counsel

set forth above (pp. 10-11) and opinion of Court of Appeals (R. 94-5). But, as we have already pointed out (pp. 7-9 above), if this were the motive for the 1932 amendment, it would be expected that the Legislature would have followed the course taken by it on two previous occasions in meeting similar situations, *viz.*, to provide that, upon the exercise of the power after the enactment of the new law, the property subject to the power should be treated in the same way as if the power had not been exercised, or had been exercised by a non-resident, *i.e.*, the old legacy tax should be imposed in respect of the property in the estate of the grantor of the power.

In any event, the most that this suggested possible reason of policy would have justified was the restoration of the tax which had been inadvertently repealed; it could not possibly be regarded as justifying the imposition of a new and different tax based upon an erroneous and arbitrary factual assumption and producing the oppressive and discriminatory effect which has been set forth.

It will not do to urge that it was easier to impose the new estate tax than to restore the old legacy tax. Even if there were any factual basis for such a claim, it is clear that such an attempted justification would not meet with the approval of this Court. Thus, in *Stewart Dry Goods Co.* v. *Lewis*, 294 U. S. 550 (1935), the Court, through Mr. Justice Roberts, said (pp. 559-60):

> "We are told that the gross sales tax in question is in truth a rough and ready method of taxing gains under the guise of taxing sales; that it is less complicated and more convenient of administration than an income tax; and Ken-

> tucky for these reasons is at liberty to choose this form, and to ignore the consequent inequalities of burden in the interest of ease of administration. *The argument is in essence that it is difficult to be just, and easy to be arbitrary. If the Commonwealth desires to tax incomes it must take the trouble equitably to distribute the burden of the impost.* Gross inequalities may not be ignored for the sake of ease of collection." (Italics supplied.)

It must certainly be true that even in an effort to close a loophole in a tax statute, a State may not completely ignore the equal protection requirement to which it is subject in all other fields of action, and that is precisely what has been done in the present case.

POINT III

THE APPLICABILITY OF THE STATUTE ONLY TO NON-GENERAL POWERS OF APPOINTMENT CREATED BEFORE SEPTEMBER 1, 1930, CONSTITUTES AN ADDITIONAL GROUND OF INVALIDITY UNDER THE EQUAL PROTECTION CLAUSE.

The statute prescribes a chronological classification of a kind which has been held by this Court to constitute a denial of the equal protection of the laws.

Subdivision 7-a of Section 249-r of Article 10-C of the New York Tax Law, which was added by the 1932 amendment involved in the present case, requires the inclusion in the decedent's taxable estate of property "passing under" a non-general power of appointment exercised by the decedent *only if*

> "the transfer of such property is not or was not subject to a death tax in the estate of the grantor of such power * * *."

Upon the enactment of Article 10-C, effective September 1, 1930, all appointive property became subject to a death tax (*i.e.*, the new estate tax) in the estate of the grantor of the power, since such property is as much a part of the grantor's estate for the purpose of the new tax as any of his other property. Consequently, it is clear that the applicability of subdivision 7-a depends on whether the power of appointment involved was created before September 1, 1930, in which case subdivision 7-a may apply, or after September 1, 1930, in which case subdivision 7-a can never apply.*

Thus, under the statute here in question, property subject to a non-general power is aggregated with the property of the *grantee* for the purpose of determining the tax if the power was created before September 1, 1930, whereas if the power was created after that date, such property is aggregated with the other property of the *grantor* of the power. This Court has squarely held that such a difference in treatment, based solely on the date when the power was created, constitutes an arbitrary and capricious classification which is violative of the equal protection clause. *Binney* v. *Long*, 299 U. S. 280 (1936).

In the *Binney* case, a Massachusetts death tax statute of the legacy tax type was involved. Effective September 1, 1907, Massachusetts had enacted a legacy tax statute which treated property subject to powers of appointment as being received by the beneficiary from the grantor of the power, not the grantee. Under this

* Between April 2, 1925 and September 1, 1930, Article 10-B of the New York Tax Law was operative, and under that Article appointive property was subject to a death tax in the estate of a resident grantor of a power, not in all cases, but whenever his net estate was of a certain minimum value, as prescribed in Article 10-B.

statute, if the grantor of the power had died before September 1, 1907, no legacy tax at all was payable in respect of the property subject to the power.

In 1909, Massachusetts enacted an amendment to the effect that property subject to a power of appointment should be taxed, on the exercise or non-exercise of the power, as if the property had been the property of, and had been received from, the grantee of the power. It was provided, however, that this amendment was to apply only to powers of appointment created (either by deed or by will) prior to September 1, 1907 (when the legacy tax statute first became effective); it was not to apply to powers created after that date.

In the case before the Court, the decedent had died intestate in 1931, and at her death was the grantee of two powers of appointment, one created in 1862 by an *inter vivos* deed of her father, and the other created in 1891 by the will of her mother. The property subject to each of these powers had been held taxable under the amended statute above described, and in accordance with another provision of the statute, such property had been aggregated with other property of the decedent going to the same beneficiaries in computing the rates of tax applicable under the progressive rate scale.

The Court held that, as so applied, the Massachusetts statute contravened the equal protection clause. The basis of the decision was that it was arbitrary and discriminatory for Massachusetts to make transfers by the exercise or non-exercise of a power of appointment taxable in the estate of the grantee of the power if the power was created prior to 1907, and not taxable in the estate of the grantee of the power if the power was created subsequent to 1907.

The Court took up separately the 1862 trust and the 1891 trust. In connection with its discussion of the former, the Court, through Mr. Justice Roberts, said (pp. 289-90):

> "The law, therefore, creates two classes,—the one composed of beneficiaries who take at the death of the donee of a power created by an instrument antedating 1907, who are taxed,—and the other of beneficiaries who take in succession to the donee of a power conferred by a deed executed subsequent to 1907, who are not taxed. Upon its face the statute arbitrarily selects a past date, taxing the beneficiaries of an act if done prior to, and leaving untaxed beneficiaries of a precisely similar act if done subsequent to that date. (p. 289)
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> * * * * * *
>
> "Neither the appellee nor the Supreme Judicial Court advances any satisfactory reason for this difference in treatment of persons similarly circumstanced." (p. 290)

In connection with its discussion of the 1891 trust, the Court said (p. 293):

> "We think it an arbitrary and unreasonable discrimination that the beneficiary of a power must aggregate the interest so derived with that enjoyed by inheritance of property owned in fee by the donee of the power, if the instrument creating the power antedates 1907, but need not so aggregate the interests for the purpose of taxation if the creation of the power be subsequent to 1907. The consequence that the one must pay at a higher rate on the interest falling in at the death of the donee of the power than the other who takes by reason of an exactly sim-

ilar event, denies the equal protection of the law to the former."

In the present case, subdivision 7-a, enacted in 1932, can apply only to powers created prior to September 1, 1930, and can never apply to powers created after September 1, 1930; just as in the *Binney* case the statute in question, enacted in 1909, applied only to powers created prior to September 1, 1907, and not to powers created after September 1, 1907. The decision in the *Binney* case that the attempted classification in the Massachusetts statute was arbitrary and discriminatory, is equally applicable to the identical classification attempted in the New York statute here under consideration.

The fact that the date, September 1, 1907, was specifically mentioned in the Massachusetts statute involved in the *Binney* case, while the date, September 1, 1930, is not specifically mentioned in subdivision 7-a, surely cannot make any possible difference on the question whether the classification is arbitrary. It is just as clear that subdivision 7-a does not apply to powers created after September 1, 1930, as if the date had been specifically mentioned; and the equal protection clause deals with substance rather than form.

The Court of Appeals suggests in its opinion (R. 99-100) that in the *Binney* case, the discrimination was improper because it was based on a date arbitrarily selected, whereas in the present case, the discrimination is not arbitrary because it is based upon a date selected in order to prevent transfers "thereafter effected under powers theretofore granted from escaping all taxation". But it is clear that in the case of the Massachusetts statute involved in the *Binney* case, the

reason for the exemption of powers created after September 1, 1907 was that, from that date on, there was a death tax statute in force reaching the property subject to the power in the estate of the grantor of the power, just as in the present case there was, from September 1, 1930 on, such a death tax statute in force. Indeed, the justification for the selection of the date which is suggested by the Court of Appeals here was urged by the appellee Commissioner in the *Binney* case (see brief for appellee, No. 77, October Term, 1936, at pp. 32-3).

The one point of difference between the two cases, namely, that the present case involves an estate tax rather than a legacy tax, merely serves to aggravate the discrimination in the present case. Under the Massachusetts statute, the aggregation of the appointive property with other property for the purpose of the graduated rate provisions, to which the Court in its opinion in the *Binney* case adverted, was only an aggregation with other property going to *the same beneficiary*. In the present case, the effect of applying subdivision 7-a has been to aggregate the appointive property with all of the other property comprising the decedent's taxable estate, not only the property going to the same beneficiaries, but also all of the property going to entirely different beneficiaries. Thus, the injustice and inequalities produced by the aggregation in the present case are even more striking than in the *Binney* case.

CONCLUSION

The best that can be said of the 1932 amendment is that it is an inadvertent excrescence on an otherwise rational system of death taxation. It can be invali-

dated without in any way affecting the remainder of the statute. It cannot even be supposed that any substantial loss of revenue to the State would result from its elimination. For it could hardly be expected that if the present tax is sustained, any grantee of a special power of appointment created before 1930 would hereafter exercise such power and thereby cast upon those who succeed to his own estate an additional tax burden unrelated to any benefit or privilege enjoyed by either the grantee or his heirs.

The inevitable result of permitting the statute to stand will be the frustration, in an indeterminate number of cases, of the wholly laudable purpose of some decedent who died before 1930 to have some survivor determine how his property should best be apportioned among the objects of his bounty in the light of circumstances subsequent to his death.

Nor is it necessary to assume that the invalidation of the 1932 amendment will result in permitting property subject to powers created before 1930 to escape all death taxation upon the subsequent exercise of the powers. It may properly be assumed that when the arbitrary and discriminatory nature and effect of the 1932 amendment are brought home to the Legislature by a decision of this Court invalidating the statute, the Legislature will promptly take the rational course of restoring in respect of such property the legacy tax inadvertently repealed upon the enactment of Article 10-C in 1930.

THE STATUTE HERE INVOLVED AS APPLIED IN THE PRESENT CASE DEPRIVES THE APPELLANTS OF THEIR PROPERTY WITHOUT DUE PROCESS OF LAW AND DENIES TO THEM THE EQUAL PROTECTION OF THE LAWS, AND ACCORDINGLY THE JUDGMENT OF THE STATE COURT SHOULD BE REVERSED.

Respectfully submitted,

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